

SBA's West Virginia District Office Presents SBA 7(a) PARRiS Overview

April 4, 2017

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SBA 7(a) PARRiS Overview

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PARRiS Score Objectives

The objective of the PARRiS Scorecard is to provide lenders a risk framework with attribute benchmarks that

- accurately measure lender risk, are fair, systematic, easy to understand, and on par with industry standards;
- identify the underperforming lenders to assist SBA's Office of Credit Risk Management (OCRM) in resource allocation;
- and help lenders identify areas to improve and understand their target ranges and the metrics on which SBA will score their performance.

PARRIS Score Basics

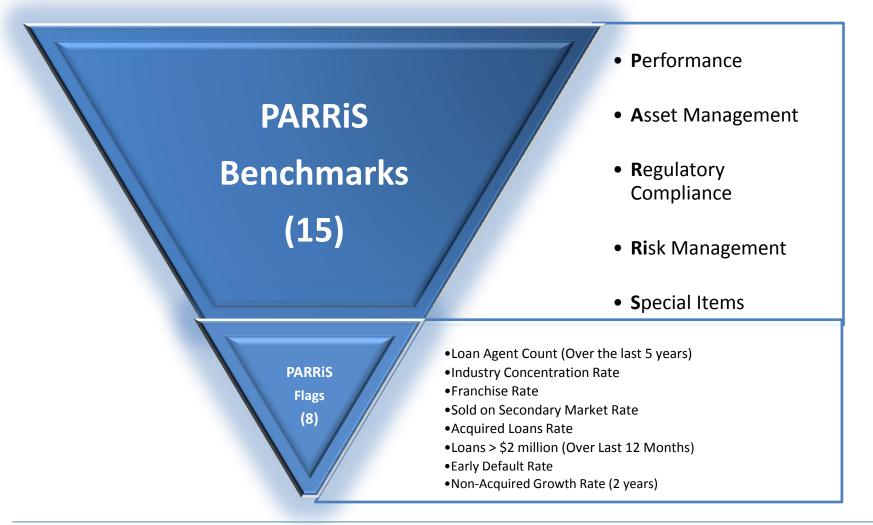
The PARRiS score is calculated from 15 benchmarks, which are classified into five categories.

• Performance, Asset Management, Regulatory Compliance, Risk Management and Special Items.

Each of the 15 benchmarks is assigned a score.

- The sum of all 15 benchmark scores equals the lender's overall PARRiS score.
 - The lender's score will be updated on a quarterly basis, with an overall score range of 15 75.
 - Eight flags, which highlight *potential* lender risk, are not included in the PARRiS score calculation.

PARRiS Risk Framework





PARRiS Methodology

One benchmark scorecard is established for all lenders.

A"20/60/20" rule is used to establish the *higher risk* (+5), *moderate risk* (+3), and *lower risk* (+1) thresholds.

The "Lower Risk" threshold uses the best 20th percentile of 2005 lender performance data.

• 2005 was a period of time when the overall economy was stable and the 7(a) program was essentially subsidy neutral (net cash yields close to zero) and thus is the lower risk state of performance.

The "Higher Risk" threshold is defined with the worst 20th percentile of current 2015Q4 lender performance data.

This approach enables SBA to encourage lenders to minimize risky behavior, while still accounting for the post recession environment.

The risk ranking methodology for the overall PARRiS score (e.g. score ranges considered "high", "medium", or "low" risk) is currently in the works.

PARRiS's 2016 Q4 Update

The overall objective of the 2016Q4 PARRiS update is to increase the usefulness, relevancy, and intuitiveness of the lender risk framework

The update will encompass the below <u>2 changes</u>:

- 1. Re-calibrating the high risk thresholds to better align with 2016 lending environment
 - The higher risk thresholds were originally created based off of 2013 lender performance data to take into account the residual effects of the Great Recession
 - Since this time the performance of the overall 20th percentile have been volatile and for the most part have improved. Thus the higher risk benchmarks have been recalibrated to meet this changing environment.
- 2. Re-structuring PARRiS by replacing certain metrics with more applicable rates
 - The Lender Purchase Rating has been replaced with the Forecasted Purchase Rate which will result in more granularity as it is the basis for the LPR.
 - The 5 Year Recovery Rate has been replaced with the 5 Year Charge Off Rate which is a more useful performance metric and better reflects the SBA's evaluation factors.



PARRiS Scorecard

Green boxes indicate an improvement in behavior between 2013 and 2016, while red boxes indicate a degradation in behavior.

Updated Scorecard

Current Thresholds

PARRIS Category	Attribute	Lower Risk	Moderate Risk (+3)	Higher Risk (+5)		Higher Risk (+5)
	5 Year Cumulative Net Yield	> 2%	≥ -1% AND ≤ 2%	< -1 %		< -3 %
Performance	12 Month Default Rate	0%	> 0% AND ≤ 4%	> 4%		> 6%
	5 Year Default Rate	0%	> 0% AND ≤ 4%	> 4%		> 5%
	Stressed Loan Rate	0%	> 0% AND ≤ 3%	> 3%		> 5%
Asset Management	Early Problem Loan Rate	0%	> 0% AND ≤ 4%	> 4%		> 2%
	High Risk Origination Rate	< 7%	≥ 7% AND ≤ 18%	> 18%		>18%
D. andata ma	Loans in Default Status over 3 Years Rate	< 19%	≥ 19% AND ≤ 60%	> 60%		> 63%
Regulatory	24 Month Repair/Denial Rate	0%	> 0% AND ≤ 3%	> 3%		> 4%
Compliance	1502 Reporting Rate	100%	≥ 97% and < 100%	< 97%		< 97%
	Prim. Fed Fin. Inst. Regulator Total Risk Based Capital Ratio	≥ 10%	< 10% AND ≥ 8%	< 8%		< 8%
Risk Management	Non-Performing Asset Ratio	((+ 5)		(+ 5)	
	Tron's choming / issee Ratio	<	< 100 %			≥100%
	Forecasted Purchase Rate (FPR)	< 0.5%	≥0.5% AND ≤ 3%	> 3%		n/a
	Average Portfolio SBPS (weighted for \$)	> 203	≤ 203 AND ≥ 180	< 180		< 181
Special Items	5 Year Charge Off Rate	0%	> 0% AND ≤10 %	> 10%		n/a
Special Items	Public Corrective Action/ No Prudential	((+1)			(+ 5)
	Regulator		No	Yes		Yes

PARRiS Benchmark Definitions: Performance

PARRIS Category	Attribute	Lower Risk (+I)	Moderate Risk (+3)	Higher Risk (+5)	Description
	5 Year Cumulative Net Yield	> 2%	≥ -1% AND ≤ 2%	< -1 %	Numerator - (Annualized) Cumulative net cash flow, including purchase, recovery, origination and servicing fees Denominator - SBA's guarantee share of the gross balance averaged over the last 5 years
Performance	12 Month Default Rate	0%	> 0% AND ≤ 4%	> 4%	Numerator - Default Amount over the last 12 months, defined by transfer to liquidation amount or gross purchase amount Denominator - Active Gross Balance due to regular servicing averaged over the last 12 months + the Default Amount over the last 12 months
	5 Year Default Rate	0%	> 0% AND ≤ 4%	> 4%	Numerator - (Annualized) Default Amount over the last 5 years, defined by transfer to liquidation amount or gross purchase amount Denominator - Active Gross Balance due to regular servicing averaged over last 5 years + Default Amount over last 5 years

PARRIS Benchmark Definitions: Asset Management

PARRIS Category	Attribute	Lower Risk (+I)	Moderate Risk (+3)	Higher Risk (+5)	Description
	Stressed Rate	0%	> 0% AND ≤ 3%		Numerator - Stressed (past due (31-59 days past due), deferred, delinquent (60 or more days past due)) balance Denominator - Active Gross Balance due to regular servicing
Asset Management	Early Problem Loan Rate	0%	> 0% AND ≤ 4%	> 4%	Numerator - Active Gross Balance for young (mob ≤ 36) loans that have had either a deferred, delinquent (60 or more days past due), liquidated, purchased, or charged off status within 18 months of disbursement Denominator - Gross Approval Amount for young loans (mob ≤ 36)
	High Risk Origination Rate	< 7%	≥ 7% AND ≤ 18%	> 18%	Numerator - Gross Approval Amount for young (mob ≤ 36) risky (original SBPS < 160) loans* Denominator - Gross Approval Amount for young loans (mob ≤ 36)

PARRiS Benchmark Definitions: Regulatory Compliance

PARRIS Category	Attribute	Lower Risk (+1)	Moderate Risk (+3)	Higher Risk (+5)	Description
	Loans in Default Status over 3 Years Rate	< 19%	≥ 19% AND ≤ 60%	> 60%	Numerator - Gross Balance of loans in active default status over 3 years Denominator - Gross Balance of all loans currently in active default
Regulatory Compliance	24 Month Repair/Denial Rate	0%	> 0% AND ≤ 3%	> 3%	Numerator - Last 24 months repair, denial, or voluntary Purchase Amount Denominator - Gross SBA Purchase Amount
	1502 Reporting Rate	100%	≥ 97% and < 100%	< 97%	Numerator - Number of active reporting loans Denominator - Total active loans in lender's SBA portfolio

PARRiS Benchmark Definitions: Risk Management

PARRIS Category	Attribute	Lower Risk (+I)	Moderate Risk (+3)	Higher Risk (+5)	Description
	FDIC Total Risk-Based Capital Ratio	≥ 10%	< 10% AND ≥ 8%	< 8%	FDIC Benchmark explanations and definitions can be found here: http://www.fdic.gov/regulations/safety/manual/section2-I_toc.html
			(+1)	(+5)	Description
	Non-Performing Asset Ratio	< 100 %		≥100%	Nonperforming assets plus loans 90 or more days past due as a percent of tangible equity and reserves. This is commonly known as the Texas Ratio (FDIC).
Risk Management	Forecasted Purchase Rate	< 0.5%	≥ 0.5% and ≤ 3%	> 3%	A 7(a) Lender's portfolio-level purchase probability over the next 12 months. SBA assigns each SBA-guaranteed active loan a projected purchase rate (PPR) using a unique set of factors that SBA has determined to be predictive for that type of loan (see SBA Notice of Revised Lender Risk Rating System, published in Federal Register Vol 79, No. 82 April 29, 2014). Each individual loan-level PPR is then multiplied by the total outstanding balance of the loan. The sum of all of those values is an estimation of the total purchase dollars for the 7(a) Lender's SBA portfolio in the next 12 months. That estimate is then divided by the total outstanding balance of all loans in the above calculation to obtain the SBA 7(a) Lender's Forecasted Purchase Rate.

P	Previous Risk	Lender Purchase Rating (formerly	1.2	2	4 5	A Landay Pating based on forecasted purchases for the payt 12 months
Man	nagement Metric	LRR)*	1, 2	3	4, 5	A Lender Rating based on forecasted purchases for the next 12 months

^{*}Lender Purchase Rating is an old metric that was removed in Q4 2016, but is scored for any historical PARRiS score before then.



PARRiS Benchmark Definitions: Special Items

PARRIS Category	Attribute	Lower Risk (+1)	Moderate Risk (+3)	Higher Risk (+5)	Description
	Average SBPS (weighted) > 203 ≤ 203 AND ≥ 180	< 180	Average Small Business Risk Portfolio Solution (SBPS) Score) weighted by the		
		> 203	3 203 AND 2 100	100	outstanding balance of scored loans (active regular servicing and liquidated)
Special Items Public C	5 Year Charge Off Rate	0%	> 0% AND ≤ 10%	> 10%	Numerator - The gross charge-off amount occurred over the past 60 months. Denominator - The gross charge-off amount occurred over the past 60 months plus the outstanding gross balance
	Public Corrective Action or No		(+1)	(+5)	Description
	Prudential Regulator		No	Yes	The occurrence of a public corrective action plan or the lack of a Prudential Regulator

Previous Special Items Metric Recovery Rate (Over	- last 5 years)* >63%	≥ 21% AND ≤ 63%	< 21%	Numerator - Cumulative Recovery Amount (funds realized after purchase) for defaulted loans charged off or paid in full over the last 5 years Denominator - Cumulative Default Amount for loans charged off or paid in full over last 5 years
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^{*5} Year Recovery Rate is an old metric that was removed in Q4 2016, but is scored for any historical PARRiS score before then.



PARRiS Benchmark Definitions: Flags

PARRIS RISK FLAGS	Flag	Description
Loan Agent Count (Over Last 5 Years)	> 0	Number of loans originated in past 5 years using an agent
Early Default Rate	>= 1%	Numerator - The gross balance at default of young loans (mob <= 36) that experienced a default event (liquidation or purchase) when mob <= 18
% Growth Rate, Non-Acquired (2 Years)	>= 25%	Numerator - The current non-acquired loans gross balance minus the current non-acquired loans gross balance two years ago
Franchise Concentration	> 10%	Numerator - Gross balance of Franchise Dollars Denominator - Gross Balance
Sold on Secondary Market	l >75%	Numerator - Gross Balance of loans sold on secondary market Denominator - Gross Balance
Industry Concentration	> 20%	Numerator - Gross Industry Dollars of top industry concentration Denominator - Gross Balance
Acquired Loan Rate	> 25%	Numerator - Gross Balance of acquired loans Denominator - Gross Balance
Loans > \$2 Million (Over Last 12 Months)	> 5	Number of \$2M+ loans apprpoved in the last 12 months



Thank You

Contact Information

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